Supersedes: **Child Care 2-4 (5/01/05)**

References: **45 CFR 98.20; 52-2-701 - 704; 52-2-713 MCA**
ARM 37.80.201 - 202

General Rule

The gross income of all adult and minor household members is evaluated in determining household eligibility. Please refer to Household Membership in Section 2-2 'Household Requirements' of this manual.

The gross amount of income expected to be available for current use, including unearned and earned income, unless specifically excluded, is counted.

⇒ All income, even if excluded by policy, must be entered in CCUBS to ensure proper eligibility processing.

Family Shall Obtain All Income

As a condition of eligibility, each household must actively seek all income for which the household has legal claim, unless they can show good cause for not doing so. However, eligibility may not be denied if the individual did not make income information available because he/she was unaware of its existence and/or availability.

> EXAMPLE: A divorce decree/parenting plan indicates the absent parent shall pay child care until the residential parent is finished with school. Additionally, the absent parent shall pay 50% of the children's medical costs. Child support is specified separately. The residential parent shall pursue collecting child care and medical support from the obligor, which may not be collectable through CSED until a judgment is obtained.

All household income must be verified and summarized in case notes. The applicant's written or verbal statement alone is not verification.

⇒ State the type of verification and other pertinent information in Case Notes by answering the questions - who, when, what, and how.

⇒ View the document and enter the data in CCUBS. Make a copy of the document if allowable by the applicant and return the original to the applicant or participant. It is not necessary to keep a hard copy of the verification in the case file.

⇒ If verbal verification is obtained from a collateral contact, document the contact in Case Notes by answering the questions - who, when, what, how.

Verifying Unearned Income

It is the applicant's responsibility to provide verification of his/her unearned income. This verification is not limited to, but may include, any of the following sources:

- Attorney Statement;
- Bureau of Indian Affairs Records;
- Cash Income Records from Rental Property, Farm Produce, Boarders-lodgers, etc.
- Child Support Enforcement Division;
- Child Support Receipts;
- College and University Financial Aids Records;
- Correspondence on Benefits;
- Correspondence on SSA Benefits;
- County Clerk of the Court Records;
- Divorce Decree (may include child support, medical support, child care, alimony);
- Financial Institution Records;
- Income Tax Record - State & Federal;
- Insurance Company Records;
- Lodge, Club, or Fraternal Organization Record;
- Parenting Plan (may include child support, medical support, child care)
- Pension Award Notice;
- Personal Records of Contributions--Money orders or, canceled checks;
- Railroad Retirement Award Letter;
- Recipient's statement from person making a contribution (a current child support order is required for child support payments);
- RSDI Benefit Check or Award Letter;
- Social Security Administration Bendex interface (TEAMS);
- Social Security Administration Records;

- Unemployment Compensation Award letter;
- Union Records;
- Veteran's Administration;
- Veteran's Administration Award Notice;
- Workmen's Compensation Benefits Award Notice; and/or
- Workmen's Compensation Records.

Earned Income

The term earned income encompasses cash or in-kind income earned by an individual through the receipt of wages, salary, commissions, or profit from activities in which he/she is engaged as a self-employed individual or as an employee. Earned income is measured as gross earned income before any deductions such as FICA, taxes, garnishments, and cafeteria plans, etc., the individual receives. It includes earnings over a period of time for which settlement is made at one given time, as in the instance of sale of farm crops, livestock, poultry, or logging.

With reference to commissions, wages, or salary, earned income means the total amount, irrespective of personal expenses, such as income tax deductions, lunches, and transportation to and from work, and irrespective of expenses of employment which are not personal, such as the cost of tools, materials, special uniforms, or transportation to call on customers.

Verifying Earned Income

It is the applicant’s responsibility to provide verification of his/her earned income. The applicant’s income and work schedule shall be provided to the CCR&R on the Release of Information/Request for Verification (DPHHS-HCS/CC-011) form. If the employer refuses to complete the form or if the work schedule is variable, CCR&Rs may corroborate the parent’s statement with the following information:

- Bookkeeping records;
- Employer's payroll records;
- Employer’s verbal/written statement of earnings;
- Employment service records;
- Income tax returns - state/federal;
- Receipts for work-related expenses (Sole proprietorship, Partnership,

S-corporation);
- Sales/services receipts;
- State Department of Revenue;
- Tax statements;
- W-2 forms; and/or
- Wage/salary stubs.

Self-Employment

Self-employment is the act of engaging in a trade or business except as an employee. A trade or business is generally an activity carried on for a livelihood or in good faith to make a profit. However, business losses do not offset income earned as an employee.

The individual does not need to actually make a profit to be in a trade or business as long as a profit motive exists. Evaluating the regularity of activities and transactions and the production of income usually indicates this motive. Self-employment activities must be corroborated when using self employment work time to meet the minimum hourly work requirement.

Accept the participant's statement that he/she had no self-employment earnings during the relevant months, unless there is evidence to the contrary.

Self-employment businesses typically include the following:
- Sole Proprietorships, where the owner receives the profits.
- Partnerships, where profits are distributed among partners.
- S-Corporations, where profits flow through the corporate structure to the shareholder/owners.

Corporations are business entities in which the corporation receives the profits. Individuals working for corporations are considered employees, although some individuals doing work on behalf of the corporation may be self-employed. Examples of self-employed include:
- A board member, who receives payment only for board activities;
- An independent contractor; or
- An independent consultant.

Employee or Self-Employed?

An individual is not self-employed if performing services that can be controlled by an employer. If an employer-employee relationship exists (no matter what the relationship is called), the individual is not self-employed.

The source of the income and the individual's involvement in the activity from which the income is generated will determine whether it is self-employment income.

EXAMPLE: Income from rental property, including roomer/boarder income, is self-employment income unless all activities are conducted by an outside agency. If an outside agency, such as a realtor, conducts all activities involved in renting property, the proceeds are treated as unearned income.

EXAMPLE: An individual is engaged in fixing televisions and radios in his spare time. He has a shop, equipment, and tools. He advertises his business. This individual is considered self-employed in a trade or business.

Self-Employment Income

The dollar amount of gross self-employment income is determined by using as many sources as necessary to determine gross income and expenses, such as the following:

- Tax returns or business records which cover the relevant period;
- Participant's statement of estimated earnings;
- Receipts for business expenses;
- Receipts for goods and services provided; and
- A signed statement from bank.

⇒ Enter NET self-employment income in CCUBS.

EXAMPLE: Mrs. Stevens is self-employed as a sales representative. Her gross receipts for the month are $200. She claims as business expenses the wholesale price of the items she orders and expenses for 50 miles of transportation. Policy allows a flat rate per mile for business-related travel, and Mrs. Stevens does not document higher expenses.

Gross receipts = $200, retail price of items sold.

Business expenses = $80, wholesale price of items ordered.

Transportation cost = $18, to make sales and deliver orders (miles times the state rate per mile).

Calculation of Gross Self-Employment Income:
$200 -- Gross receipts
-98 -- Business expenses
$102 -- Net Self-Employment Income.

➢ EXAMPLE: Mr. & Mrs. Stevens are married and are self-employed in separate businesses. When determining income for this family, all self-employment income shall be added together, this will allow the losses of one business to offset the gains from another. After reviewing the taxes, Mr. Stevens has a loss of $4000 for the year, but Mrs. Stevens has a gain of $6000 for the year, their combined income would equal a positive $2000 for the year.

($4,000) – Mr. Stevens gross income
+$6,000 –Mrs. Stevens gross income
$2,000 combined gross income

Determining Business Expenses

With respect to self-employment, earned income means the total profit from a business enterprise, farming, etc., resulting from a comparison of the gross receipts with the business expenses, i.e., expenses directly related to producing the goods or service and without which the goods or services could not be produced.

Allowable business expenses are subtracted from the gross receipts to determine net self-employment income. Allowable expenses must directly relate to the production of income. If an expense is incurred for the business and for personal purposes, it must be divided proportionately.

EXAMPLE: If the home is used in the business, expenses can be deducted only for that part of the home that is <u>used both regularly and exclusively</u> for the business.

The following expenses are not allowable as a deduction when determining eligibility:

- Expenses derived from capital investments:
  - Depreciation (generally derived from equipment, buildings, and building improvements);
  - Schedule 179 Expense Deduction (generally equipment);
  - Amortization (generally derived from land, business start-up costs, organizational costs for partnership or corporation);
  - Depletion (generally derived from mineral property or standing timber);
  - Business Start-up Costs - The cost of starting a business is not allowed as an expense for eligibility purposes. The IRS considers start-up costs a capital expense and allows the business to amortize the expense over a period; and
  - Personal and entertainment expenses are not an allowable deduction for eligibility purposes. These expenses should not be found on a tax return.
- Payments on the principal portion of loan payments used to purchase capital assets or durable goods. (The interest portion of the loan is an allowable expense.)
- Personal expenses should not be claimed as business expenses:
  - Personal business and entertainment expenses and
  - Personal transportation.

A business typically has many different kinds of costs during the year. Some of these costs are counted as part of the investment in the business. They must be "capitalized", <u>are not allowable business expenses</u>, and are known as **capital expenditures or capital expenses.** Generally, three kinds of costs must be capitalized:

1) **Going into business**. The costs of getting started in a business before actually beginning business operations are all capital expenses. This may

include the cost of such things as advertising, travel, utilities, repairs, and employees' wages. <u>These are often the same kind of expenses that could be deducted if they occur after the business is opened.</u>

2) **Business assets.** The cost of any asset that will be used in the business for more than one year is a capital expense. There are many different kinds of business assets - for example, land, buildings, machinery, trucks, books, furniture, patents, and franchise rights.

3) **Improvements.** The costs of making improvements to a business asset are also a capital expense, if the improvements add to the value of the asset, appreciably lengthen the time it can be used, or adapt it to a different use. However, <u>normal repair costs are deducted as business expenses</u> and not capitalized. Examples of improvements are:
   - new electric wiring;
   - a new roof;
   - new floor;
   - new plumbing;
   - bricking up windows to strengthen a wall;
   - lighting improvements;
   - asbestos abatement; and
   - abatement of hazardous substances.

To distinguish between capital expenses and allowable expenses several different examples are discussed below.

Business motor vehicles. The cost of a motor vehicle purchased to use in the business is usually capitalized. Its cost can be recovered through annual deductions for depreciation. Depreciation is NOT an allowable business expense under program policy.

> NOTE: Repairs made to the business vehicle are allowable expenses. However, amounts paid for reconditioning and overhaul of business vehicles are capital expenses.

Roads and driveways. The cost of building a private road on the business property and the cost of replacing a gravel driveway with a concrete one are capital expenses which may be able to depreciate. The cost of maintaining a private road on the business property is allowable as an ordinary and necessary business expense.

Tools. Amounts spent for tools used in the business are deductible expenses if the tools wear out and are thrown away within one year from the date of purchase.

Machinery. The cost of replacing short-lived parts of a machine to keep it in good working condition and not to add to its life is allowable as an ordinary and necessary expense.

Heating equipment. The cost of changing from one heating system to another is a capital expense and not a deductible expense.